(2)

FILED
MAY 18 1994
OFFICE OF THE CLERK

No. 93-1650

IN THE

# Supreme Court of the United States

OCTOBER TERM, 1993

**IN THE MATTER OF THE ARBITRATION BETWEEN: ELJER MANUFACTURING, INCORPORATED, formerly known as HOUSEHOLD MANUFACTURING, INCORPORATED,**

*Petitioner,*

v.

**KOWIN DEVELOPMENT CORPORATION,**

*Respondent.*

**On Petition for a Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit**

## RESPONDENT'S BRIEF IN OPPOSITION

MICHAEL A. POLLARD
*Counsel of Record*
BAKER & McKENZIE
130 East Randolph Drive
Suite 2700
Chicago, Illinois 60601
(312) 861-8000

RICHARD G. OSBORN
OSBORN & ANDERSON
10990 Wilshire Boulevard
Suite 1500
Los Angeles, California 90024
(310) 479-6550

*Attorneys for Respondent Kowin Development Corporation*

Midwest Law Printing Co., Chicago 60611, (312) 321-0220

16 pp

## TABLE OF CONTENTS


| | PAGE |
|---|---|
| TABLE OF AUTHORITIES ..... | ii |
| STATEMENT OF THE CASE ..... | 1 |
| SUMMARY OF ARGUMENT ..... | 2 |
| ARGUMENT ..... | 4 |
| A. The Question Presented Is Academic Since The Arbitrator's Award Of Damages Was Supported By Substantial Evidence ..... | 4 |
| B. Eljer Has Failed To Raise An Important Question Meriting *Certiorari* ..... | 6 |
| C. Eljer Is Impermissibly Seeking Review On *Certiorari* Of State Law Regarding Benefit Of The Bargain Damages ..... | 9 |
| D. The Court Of Appeals' Decision Here Will Neither Undermine Confidence In Arbitrations Nor Discourage Their Use ..... | 10 |
| CONCLUSION ..... | 12 |

## TABLE OF AUTHORITIES


| *Cases* | PAGE |
|---|---|
| *Advest, Inc. v. McCarthy*, 914 F.2d 6 (1st Cir. 1990) | 8 |
| *Detroit Coil Co. v. International Association of Machinists & Aerospace Workers*, 594 F.2d 575 (6th Cir. 1979), *cert. denied*, 444 U.S. 840 (1979) | 7 |
| *Executive Life Insurance Co. v. Alexander Insurance, Ltd.*, 999 F.2d 318 (8th Cir. 1993) | 8 |
| *Flast v. Cohen*, 392 U.S. 83 (1942) | 6 |
| *Flender Corp. v. Techna-Quip Co.*, 953 F.2d 273 (7th Cir. 1992) | 11, 12 |
| *GHK Associates v. Mayer Group, Inc.*, 274 Cal. Rptr. 168 (Cal. App. 1990) | 9 |
| *Gunther v. San Diego & A.E.R. Co.*, 382 U.S. 257 (1965) | 7 |
| *Hallmark Insurance Administrators v. Colonial Penn Life Ins. Co.*, 697 F. Supp. 319 (N.D. Ill. 1988), *aff'd*, 990 F.2d 984 (7th Cir. 1993) | 9 |
| *Jenkins v. Prudential-Bache Securities, Inc.*, 847 F.2d 631 (10th Cir. 1988) | 8 |
| *Lee v. Chica*, 983 F.2d 883 (8th Cir. 1993), *cert. denied*, 114 S. Ct. 287 (1993) | 7 |
| *McIlroy v. PaineWebber, Inc.*, 989 F.2d 817 (5th Cir. 1993) | 8 |
| *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Bobker*, 808 F.2d 930 (2d Cir. 1986) | 7 |
| *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 105 S. Ct. 3346, 84 L. Ed. 2d 444 (1985) | 11 |

*National Railroad Passenger Corp. v. Chesapeake and Ohio Ry. Co.*, 551 F.2d 136 (7th Cir. 1977) . 7

*Raiford v. Merrill Lynch, Pierce, Fenner & Smith*, 903 F.2d 1410 (11th Cir. 1990) ..... 8

*Shearson Hayden Stone, Inc. v. Liang*, 653 F.2d 310 (7th Cir. 1981) ..... 7

*Stroh Container Co. v. Delphi Industries, Inc.*, 783 F.2d 743 (8th Cir. 1986), *cert. denied*, 476 U.S. 1151 (1986) ..... 7

*United Paperworkers International Union, AFL-CIO, et al. v. Misco, Inc.*, 484 U.S. 29, 108 S. Ct. 364, 986 L. Ed. 286 (1987) .. 3, 4, 6, 7, 10, 11

*United Steelworkers of America v. Enterprise Wheel & Car Corp.*, 363 U.S. 593, 80 S. Ct. 1358, 4 L. Ed. 2d 1424 (1960) ..... 6, 7

*Volt Information Sciences v. Leland Stanford Jr. University*, 489 U.S. 468, 109 S. Ct. 1248, 103 L. Ed. 2d 488 (1989) ..... 11

*Western Employers Insurance Co. v. Jefferies & Co.*, 958 F.2d 258 (9th Cir. 1992) ..... 11

*Wilko v. Swan*, 346 U.S. 427, 74 S. Ct. 182, 98 L. Ed. 168 (1953), *overruled on other grounds*, 490 U.S. 477 (1989) ..... 7, 8

*Other Authorities*

U.S. Const., Article III ..... 6

9 U.S.C. § 1 *et seq.* ..... 2

No. 93-1650

IN THE

# Supreme Court of the United States

OCTOBER TERM, 1993

**IN THE MATTER OF THE ARBITRATION BETWEEN: ELJER MANUFACTURING, INCORPORATED, formerly known as HOUSEHOLD MANUFACTURING, INCORPORATED,**

*Petitioner,*

v.

**KOWIN DEVELOPMENT CORPORATION,**

*Respondent.*

**On Petition for a Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit**

## RESPONDENT'S BRIEF IN OPPOSITION

Respondent Kowin Development Corporation and Winston and Dorothy Ko, as successors-in-interest to Kowin Development Corporation (collectively "Kowin") hereby oppose the petition of Eljer Manufacturing, Inc. ("Eljer"), for a writ of *certiorari* to the United States Court of Appeals for the Seventh Circuit ("Petition").

## I. STATEMENT OF THE CASE

Eljer's "Statement of the Case" is misleading and incomplete. Eljer incorrectly asserts that the Court of Appeals "declined to review that part of the award [involv-

ing future lost profits]." (Petition, p. 4.) As indicated subsequently, however, the Court of Appeals, while acknowledging that it was prohibited from reviewing the arbitration award for sufficiency of evidence (Opinion, App. p. 10),[1] nevertheless reviewed the evidence and thereby concluded that the evidentiary record "was clearly sufficient to support the award". (*Id.*)

It is also disingenuous for Eljer to represent that "the sole basis for the arbitrator's award was a one page five year sales and profit projection for the Joint Venture [which] no one in the proceeding could identify" (Petition, p. 5); and that "Kowin presented no evidence supporting its 15 year extrapolation [of lost profits]" (*id.*, p. 6). To the contrary, as indicated subsequently (*see* Section III A., *infra*), the arbitrator's award was not only supported by "clearly sufficient" evidence, in the words of the Court of Appeals, but all of such evidence was admitted *without objection* by Eljer and *without opposing evidence* offered by Eljer. Furthermore, the five year sales and profit projection disparaged by Eljer was, according to the evidence, prepared by Household and authenticated by witnesses. (*Id.*)

## II. SUMMARY OF ARGUMENT

By its petition for *certiorari*, Eljer seeks review by the Supreme Court of only one issue, *i.e.*, whether an arbitration award under the Federal Arbitration Act, 9 U.S.C. sections 1 *et seq.* (the "Act") is subject to judicial review

---

[1] The text of the Court of Appeals opinion is reprinted in Eljer's Petition beginning at page 1 of the Appendix. For purposes of convenience and consistency, citations to the opinion refer to the page number in Eljer's Appendix, *i.e.*, "Opinion, App. p. ____."

for insufficient evidence. Kowin contends that Eljer's petition should be denied for the following reasons:

1. As previously determined by the District Court and the Court of Appeals, the arbitrator's award of damages was supported, in the words of the Court of Appeals, by "clearly sufficient" evidence and, accordingly, the Supreme Court will have no occasion to reach the only federal question raised by Eljer in its Petition. (*See* Section III A., *infra.*)

2. Eljer has not, and cannot, demonstrate that its Petition raises any important federal question which has not previously been addressed by the Supreme Court. This Court has previously opined that an arbitration award under the Act is not reviewable for insufficiency of evidence. *United Paperworkers International Union, AFL-CIO et al. v. Misco, Inc.*, 484 U.S. 29, 38, 108 S. Ct. 364, 986 L. Ed. 286 (1987). (Section III B., *infra.*) There is no post-*Misco* relevant conflict in principle among the circuits with respect to the scope of judicial review. (*See* Section III B., *infra.*)

3. In deference to non-judicial dispute resolution, the Supreme Court has routinely denied petitions for *certiorari* raising similar issues. (*See* Section III B., *infra.*)

4. Eljer is impermissibly seeking review on *certiorari* of state law principles regarding benefit-of-the-bargain damages. Essentially, Eljer claims that the arbitrator erred by allegedly awarding speculative lost profits in a new enterprise which, according to Eljer, were unavailable under applicable state law. The Court of Appeals properly rejected this argument by observing that a state law exception to the "new business rule" obtained in this case. The application of such state law principles does not involve a federal question. Moreover, any error of law com-

mitted by the arbitrator with respect to the application of such principles would not be reviewable. *See Misco*, 484 U.S. at 38. (*See* Section III C., *infra.*)

5. The decision by the Court of Appeals does not establish novel principles and will not inhibit arbitration. The Court of Appeals' decision applied principles of review based upon decisions of this Court and the circuits which have been in the public domain for years. There is no evidence whatever to suggest that this case is unique, unprecedented or controversial. Indeed, Eljer seeks to expand judicial review to facilitate inquiry as to the sufficiency of arbitration evidence, an enterprise which will deter, rather than encourage, arbitration under the Act. (*See* Section III D., *infra.*)

## III. ARGUMENT

### A. The Question Presented Is Academic Since The Arbitrator's Award Of Damages Was Supported By Substantial Evidence.

All of the arguments presented by Eljer in its Petition are predicated upon the false premise that the arbitrator's award of lost profits was not supported by *any* evidence. It is astonishing that Eljer persists in the assertion that the lost profits award of the arbitrator was not supported by any evidence despite the incontrovertible record to the contrary. As stated by the Court of Appeals in its opinion:

> In fairness to the arbitrator, even if we could vacate the award we would not do so because the evidence was clearly sufficient to support the award. Kowin's claim for lost profits was based on Eljer's own representations about the venture's profitability and based on the purchase of a certain number of files every year.

(App. p. 10.)

The Court of Appeals' conclusion was amply supported by the record. The arbitration evidence respecting lost profits included: The Joint Venture Agreement and Sales Agreement, which specifically required the purchase of 34.67 million files during the first five years of the Joint Venture (R 42-6 at HX 21);[2] the profit projection prepared by Household over the first five year period (*Id.*, at HX 12); Household's marketing plan, which projected market increases worldwide of 2 percent to 3 percent from the sixth to twentieth year of the Joint Venture (*Id.*, at HX 1); production forecasts indicating Joint Venture production capacity of 20 million steel files per annum (*Id.*, at KX 22, pp. 13-14); representations of 21 percent profits on Chinese sales and 47 percent profits on worldwide sales outside of China (*Id.*, KX 22, p. 14); production cost accounting figures (*Id.*, KX 22, pp. 25-26); representations of net profits equal to U.S.$9,161,500 for the first five years and annual net profits thereafter of U.S.$2,000,000 for "each party" from the fifth year onward (*Id.*, KX 22, p. 27); detailed "annual profit" analysis (*Id.*, KX 22, pp. 30-32); and uncontested evidence that all financial figures and projections were provided by Household (R 42-1 at RT 126:5-16, 63:18-64:16). Indeed, Household represented that it could purchase all the files the Joint Venture was capable of producing. (R 42-1 at RT 91:19-93:6, 132:6-133:4; R 42-6 at KX 22, p. 10.)

Eljer failed to produce *any* contrary evidence. It never suggested *any* alternative to the amount of lost profits sought by Kowin. Eljer merely challenged the recoverability, as a matter of law, of benefit of the bargain damages;

---

[2] Evidentiary citations are to the record before the Court of Appeals and follow the convention used by the parties in their appellate briefs.

Eljer did not challenge the computation of the amount or the sufficiency of the evidence to support an award. This Court has consistently held that arbitration awards are not reviewable under the Act for mere error of law. *United Paperworkers International Union, AFL-CIO, et al. v. Misco, Inc.*, 484 U.S. 29, 38, 108 S. Ct. 364, 986 L. Ed. 286 (1987).

It is obvious, therefore, that Eljer proposes to seek *certiorari* for the review of issues which are irrelevant to this record. This Court would have no occasion to consider these issues unless it first determined that the lost profits award in this case was not supported by any evidence. Since there was not only some evidence but, in the Court of Appeals' words "clearly sufficient" evidence, Eljer is effectively asking this Court to render an impermissible advisory opinion. U.S. Const. Art. III; *Flast v. Cohen*, 392 U.S. 83, 96 (1942).

**B. Eljer Has Failed To Raise An Important Question Meriting *Certiorari*.**

This Court has already ruled dispositively with respect to the sole issue raised by Eljer, *i.e.*, whether an arbitration award under the Act is reviewable for insufficient evidence.

For example, this Court has held that an award under the Act is not subject to judicial review for errors of law or fact (*Misco*, 484 U.S. at 38); that the award must draw its essence from the arbitration agreement (*id.*, 484 U.S. at 36, *citing United Steelworkers of America v. Enterprise Wheel & Car Corp.*, 363 U.S. 593, 597, 80 S. Ct. 1358, 4 L. Ed. 2d 1424 (1960)); and that the arbitrator is not empowered to "dispense his own brand of industrial justice" (*id.*). These principles are equal to the task here and compel the conclusion that the Court of Appeals did not commit error in affirming the arbitrator's award of lost profits.

The Supreme Court has repeatedly denied *certiorari* to clarify further the standards of review under the Act. Of the fifteen cases cited by Eljer to evidence what it characterizes as "existing disarray in the circuits", eight were decided before this Court's decision in *Misco, supra.*[3] This Court was asked to grant *certiorari*, but declined, three times.[4] Eljer even cites the decisions of this Court in support of the proposition that *certiorari* is required in order to clarify the alleged confusion among the circuits.[5]

Post-*Misco* circuits have in effect examined arbitrations under the Act to determine if the arbitrator "dispensed his own brand of justice" or acted beyond his powers under the standards of review previously confirmed by the Supreme Court. *See United Steelworkers of America v. Enterprise Wheel & Car Corp.*, 363 U.S. 593, 597, 80 S. Ct. 1358, 4 L. Ed. 2d 1424 (1960). The circuits have applied these principles by inquiring whether the award was "completely irrational" or "unfounded in reason and fact"

---

[3] *See Shearson Hayden Stone, Inc. v. Liang*, 653 F.2d 310 (7th Cir. 1981); *National Railroad Passenger Corp. v. Chesapeake and Ohio Ry. Co.*, 551 F.2d 136 (7th Cir. 1977); *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Bobker*, 808 F.2d 930 (2d Cir. 1986); *Gunther v. San Diego & A.E.R. Co.*, 382 U.S. 257 (1965); *Stroh Container Co. v. Delphi Industries, Inc.*, 783 F.2d 743 (8th Cir. 1986); *United Steelworkers of America v. Enterprise Wheel & Car Corp.*, 363 U.S. 593 (1960).

[4] *See Detroit Coil Co. v. International Association of Machinists & Aerospace Workers*, 594 F.2d 575 (6th Cir. 1979), *cert. denied*, 444 U.S 840 (1979) (factual irrationality); *Stroh Container Co. v. Delphi Industries, Inc.*, 783 F.2d 743 (8th Cir. 1986), *cert. denied*, 476 U.S. 1151 (1986) (nonstatutory grounds); *Lee v. Chica*, 983 F.2d 883 (8th Cir. 1993), *cert. denied*, 114 S. Ct. 287 (1993).

[5] *Wilko v. Swan*, 346 U.S. 427 (1953), *overruled on other grounds*, 490 U.S. 477 (1989); *Gunther v. San Diego and A.E.R. Co.*, 382 U.S. 257 (1965); *United Steelworkers of America v. Enterprise Wheel & Car Corp.*, 363 U.S. 593 (1960).

or necessarily involved a "manifest disregard of the law" (*McIlvoy v. PaineWebber, Inc.*, 989 F.2d 817, 820 and note 2 (5th Cir. 1993)); or was "arbitrary and capricious" (*Advest, Inc. v. McCarthy*, 914 F.2d 6, 9, and note 6 (1st Cir. 1990); or had a "rational basis" (*Jenkins v. Prudential-Bache Securities, Inc.*, 847 F.2d 631, 634 (10th Cir. 1988); or was irrational (*Raiford v. Merrill Lynch, Pierce, Fenner & Smith*, 903 F.2d 1410, 1413 (11th Cir. 1990); or failed to derive its "essence from the contract" (*Executive Life Insurance Co. v. Alexander Insurance, Ltd.*, 999 F.2d 318, 320 (8th Cir. 1993)). The descriptive phrases used by the circuits, although differing in nomenclature, are merely the rationale under which this Court's standards of review above summarized have been applied. There is no "disarray among the circuits." Rather, the circuits have predictably adopted the standards articulated by the Supreme Court to the specifics of each case. This Court has done the same. *See Wilko v. Swan*, 346 U.S. 427, 436, 74 S. Ct. 182, 98 L. Ed. 168 (1953), *overruled on other grounds*, 490 U.S. 477 (1989) (where this Court coined the phrase "manifest disregard of the law.")

In any event, the decision of the Court of Appeals in this case would be affirmed under any of the rationale in use among the circuits. Interestingly, Eljer does not maintain otherwise except in the narrow case where there is no evidence whatever to support an award. As previously indicated, however, no good faith argument can be advanced here that the award of lost profits was not supported by *any* evidence. (*See* Section II A., *supra*.)

### C. Eljer Is Impermissibly Seeking Review On *Certiorari* Of State Law Regarding Benefit Of The Bargain Damages.

Eljer seeks *certiorari* on the pretext that it is necessary for this Court to clarify the scope of judicial review under the Act, claiming that the arbitrator erred here by allegedly awarding speculative lost profits in a new enterprise which profits were, accordingly, unavailable under applicable state law. In effect, therefore, Eljer is requesting this Court to reevaluate the arbitrator's conclusion of law that lost profits were not speculative and were available in this case under state law.

The Court of Appeals properly declined to overturn the arbitrator's decision in this respect:

> Even if an arbitrator's mistake of law permitted us to modify his decision, we still would not do so here. The premise of a so-called "new business" rule is that the success of a new enterprise is ordinarily uncertain. Where, however, the enterprise is simply an absorption or extension of a previously established successful operation and the venture's future is less in doubt, the awarding of future lost profits is not, as a matter of law, forbidden. *GHK Associates v. Mayer Group, Inc.*, 274 Cal. Rptr. 168 (Cal. App. 1990); *Hallmark Insurance Administrators v. Colonial Penn Life Ins.*, 697 F. Supp. 319, 327 (N.D. Ill. 1988), aff'd. 990 F.2d 984 (7th Cir. 1993). Kowin argued that the Chinese venture fell under this exception and the arbitrator could have made his decision on this basis.

(Opinion, App. p. 9.)

Second, even if the arbitrator had committed error in construing applicable law, he did so on the basis of extensive legal arguments presented by both sides citing federal and state authority. Accordingly, it cannot be said that his rulings constituted his "own brand of industrial

justice" (*Misco*, 484 U.S. at 36), or that his implied ruling did not "draw its essence" from the arbitration agreement (*id.*). It is uniformly established, including in the Supreme Court, that arbitration awards under the Act are not reviewable for errors of law. *Misco*, 484 U.S. at 38.

Finally, it is absurd to suggest that this Court should grant *certiorari* for the purpose of resolving state law questions concerning the recoverability of benefit of the bargain damages. *Certiorari* is not available to review state law where no controlling federal question is presented. *See* Supreme Court Rule 10 (subparagraphs (a) through (c) of Rule 10.1 clearly contemplate review of "federal questions" only).

**D. The Court Of Appeals' Decision Here Will Neither Undermine Confidence In Arbitrations Nor Discourage Their Use.**

Eljer proffers no evidence whatever, nor could it do so, to support its self-serving assertion that the Court of Appeals' decision here will undermine public confidence in the arbitration process. As relevant here, the Court of Appeals' decision is based upon decisions of this Court and the circuits which have been in the public domain for years. Nevertheless, the public is resorting to non-judicial dispute resolution, including arbitrations under the Act, with increasing frequency. The Court of Appeals did not promulgate any novel standards of review.

Indeed, Eljer would have this Court grant *certiorari* for the purpose of encouraging judicial review of arbitration awards through inquiry into the sufficiency of evidence. As has been recognized by this and other courts, such an exercise would discourage, rather than promote, resort to arbitration as a simple, speedy, cost effective and final

means of resolving commercial disputes. *See, e.g., Flender Corp. v. Techna-Quip Co.*, 953 F.2d 273, 279 n. 4 (7th Cir. 1992) ("Judicial review [of arbitration awards] has been thus restricted in order to further the objective of arbitration, which is to enable the parties to resolve disputes promptly and inexpensively, without resort to litigation . . . .").

If there is some risk of uncertainty associated with the arbitration process, that is simply the risk which the parties have contractually accepted to achieve the efficiency and certainty of arbitration. It is worth noting that it was Eljer, and not Kowin, which compelled arbitration and selected the forum.

One of the significant advantages of arbitration is that the contracting parties are free to incorporate into their agreement any provisions which they believe necessary to mitigate potential uncertainty and control the activities of the arbitrator. These privately negotiated procedures must be honored by the arbitrator, and the courts. *Volt Information Sciences v. Leland Stanford Jr. University*, 489 U.S. 468, 478, 109 S. Ct. 1248, 103 L. Ed. 2d 488 (1989).

The parties are free, as in this case, to have their disputes arbitrated by mutually acceptable arbitrators. *Misco*, 484 U.S. at 37. They may exclude selected issues from the scope of arbitration (*Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 628, 105 S. Ct. 3346, 84 L. Ed. 2d 444 (1985)); or require the arbitrator to render detailed findings of fact and conclusions of law (*Western Employers Insurance Co. v. Jefferies & Co.*, 958 F.2d 258, 261 (9th Cir. 1992); or limit the nature or scope of remedies available (*Misco*, 484 U.S. at 41). Indeed, in this case the contracting parties could have specifically provided for liquidated or other forms of damage so as to obviate potential liability for lost profits; or they could

have agreed in the arbitration clause to limit the arbitrator's right to award lost profits. It is this flexibility which enhances the attraction of arbitration to commercial litigants. Judicial activism would merely inhibit the process. *Flender Corp.*, 953 F.2d at 279 n. 4.

## IV. CONCLUSION

For the foregoing reasons, it is respectfully submitted that Eljer's Petition for writ of *certiorari* should be denied.

Respectfully submitted,

MICHAEL A. POLLARD
*Counsel of Record*
BAKER & McKENZIE
130 East Randolph Drive
Suite 2700
Chicago, Illinois 60601
(312) 861-8000

RICHARD G. OSBORN
OSBORN & ANDERSON
10990 Wilshire Boulevard
Suite 1500
Los Angeles, California 90024
(310) 479-6550

*Attorneys for Respondent*
*Kowin Development Corporation*

Dated: May 18, 1994

# REPLY BRIEF

Supreme Court, U.S.
FILED
MAY 31 1994
OFFICE OF THE CLERK

(3)

No. 93-1650

IN THE

# Supreme Court of the United States

OCTOBER TERM, 1993

**IN THE MATTER OF THE ARBITRATION BETWEEN: ELJER MANUFACTURING, INCORPORATED, formerly known as HOUSEHOLD MANUFACTURING, INCORPORATED,**

*Petitioner,*

v.

**KOWIN DEVELOPMENT CORPORATION,**

*Respondent.*

**On Petition for a Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit**

## REPLY BRIEF OF PETITIONER

WILBER H. BOIES, P.C.
*Counsel of Record*
DAVID B. BAYLESS
MERCEDES A. LAING
McDERMOTT, WILL & EMERY
227 West Monroe Street
Chicago, Illinois 60606-5096
(312) 372-2000
*Counsel for Petitioner*

Midwest Law Printing Co., Chicago 60611, (312) 321-0220

11pp

## TABLE OF CONTENTS


| | PAGE |
|---|---|
| TABLE OF AUTHORITIES ..... | ii |
| REPLY BRIEF OF PETITIONER ..... | 1 |
| ARGUMENT ..... | 1 |
| I. | |
| THE QUESTION PRESENTED—WHETHER AN ARBITRATION AWARD IS REVIEWABLE TO DETERMINE IF IT IS BASED ON SUFFICIENT EVIDENCE OR IS NOT IRRATIONAL—IS NOT ACADEMIC BECAUSE THE SEVENTH CIRCUIT DID NOT HOLD THAT THE FIFTEEN-YEAR DAMAGES AWARD WAS BASED ON SUFFICIENT EVIDENCE .. | 2 |
| II. | |
| THIS COURT IN *MISCO* DID NOT DECIDE WHETHER AN ARBITRATION AWARD IS REVIEWABLE TO DETERMINE IF IT IS BASED ON SUFFICIENT EVIDENCE OR IS NOT IRRATIONAL ..... | 4 |
| CONCLUSION ..... | 8 |

## TABLE OF AUTHORITIES


| Cases | PAGE |
|---|---|
| *In re Arbitration No. AAA13-161-0511-85 under Grain Arbitration Rules*, 867 F.2d 130 (2d Cir. 1989) | 6 |
| *Mutual Fire, Marine & Inland Ins. Co. v. Norad Reinsurance Co., Ltd.*, 868 F.2d 52 (3d Cir. 1989) | 6 |
| *Pacific Reinsurance Management Corp. v. Ohio Reinsurance Corp.*, 935 F.2d 1019 (9th Cir. 1991) | 6 |
| *Storer Broadcasting Co. v. American Federation of Television & Radio Artists*, 600 F.2d 45 (6th Cir. 1979), *cert. denied*, 454 U.S. 1099 (1981) | 6 |
| *United Paperworkers International Union v. Misco, Inc.*, 484 U.S. 29 (1987) | 4, 5, 6 |

No. 93-1650

IN THE

# Supreme Court of the United States

OCTOBER TERM, 1993

**IN THE MATTER OF THE ARBITRATION BETWEEN: ELJER MANUFACTURING, INCORPORATED, formerly known as HOUSEHOLD MANUFACTURING, INCORPORATED,**

*Petitioner,*

v.

**KOWIN DEVELOPMENT CORPORATION,**

*Respondent.*

**On Petition for a Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit**

## REPLY BRIEF OF PETITIONER

Petitioner Eljer Manufacturing ("Eljer") replies to the brief of respondent Kowin Development Corporation and Winston and Dorothy Ko, as successors-in-interest to Kowin Development Corporation (collectively "Kowin"), in opposition to Eljer's petition for a writ of certiorari (the "Petition").

## ARGUMENT

The Petition asks this Court to review a judgment of the Seventh Circuit Court of Appeals which, in conflict with decisions from the Second, Third, Sixth and Ninth

Circuits, barred review of an arbitration award for sufficiency of the evidence. That part of the judgment for which Eljer seeks review—the Court of Appeals' affirmance of an extrapolation of fifteen years' lost profits from a five-year sales and profit projection—is not supported by any evidence in the record. Rather than squarely addressing the issue before this Court, Kowin mischaracterizes the Petition, misrepresents the Seventh Circuit's opinion and misstates the law of this Court and the circuits regarding the standard of review for arbitration decisions.

Aside from generalities about arbitration, Kowin's brief makes only two specific arguments about why this Court should not hear this case. First, Kowin claims that the question presented in the Petition is academic because the Seventh Circuit found that the arbitrator's award was supported by substantial evidence. Second, Kowin claims that this Court has already decided whether an arbitration award is reviewable for sufficiency of the evidence. Both of Kowin's arguments are simply wrong.

## I.

## THE QUESTION PRESENTED—WHETHER AN ARBITRATION AWARD IS REVIEWABLE TO DETERMINE IF IT IS BASED ON SUFFICIENT EVIDENCE OR IS NOT IRRATIONAL—IS NOT ACADEMIC BECAUSE THE SEVENTH CIRCUIT DID NOT HOLD THAT THE FIFTEEN-YEAR DAMAGES AWARD WAS BASED ON SUFFICIENT EVIDENCE.

Kowin claims that the issue presented by this petition is "academic" because the Court of Appeals determined that the arbitrator's award of lost profits was supported by sufficient evidence. (Kowin brief at 4-6) The Seventh Circuit's opinion refutes Kowin's position.

In the courts below, Eljer made separate and distinct challenges to the evidentiary sufficiency of the two parts of the lost profits award. Eljer argued that the $1,364,372 portion of the award stemming from a five-year profit projection was based on profoundly insufficient evidence. Eljer further contended that the $7,019,944 fifteen-year extrapolation of lost profits after that five years had *no* evidentiary support.

As its opinion makes clear, the Seventh Circuit responded separately to these arguments. The court refused to adopt sufficiency of the evidence as a ground to set aside any arbitration award; however, the court reviewed the basis for the five-year award and held that the award was supported by sufficient evidence. (*See* Opinion at App. 10 and Petition at 7) In contrast, with respect to the fifteen-year award, the Court of Appeals concluded it lacked the authority to review the award (without citation to any legal authority) and summarily affirmed the award without examination of its evidentiary basis. The court noted that "[a] question as to the sufficiency of the evidence before the arbitrator simply does not trigger the review powers of this court." (*See* Opinion at App. 10 and Petition at 8) The only question presented to this Court concerns the Seventh Circuit's holding with respect to that fifteen-year award. (*See* Petition at 8)

To confuse the issue, Kowin quotes only the Seventh Circuit's discussion of the first five years' damages and carefully avoids any mention of the very next paragraph, which concerns the fifteen-year extrapolation. (*Compare* Petition at 7-8 with Kowin brief at 4) In fact, Kowin's entire brief focuses on the five-year award, even though it is *not* the subject of the Petition.

Kowin similarly attempts to mislead this Court by asserting that the arbitration record supports the Court of Appeals' conclusion regarding sufficiency of the evidence. (Kowin brief at 5) None of the evidence Kowin proffers is directed to the fifteen-year extrapolation from the five-year projection. In any event, since the Seventh Circuit did not hold that the extrapolation was based on sufficient evidence, Kowin's recitation of record evidence misses the point.

Eljer has presented a question for review which was central to the result in this case: an award of $7 million of "future lost profits" damages without any supporting evidence. Resolution of this question is also pivotal to the outcomes of the future arbitrations which are submitted for judicial review in the Seventh Circuit and other circuits. Eljer respectfully asks this Court to reject Kowin's attempts at obfuscation and to review the judgment of the Seventh Circuit.

## II.

## THIS COURT IN *MISCO* DID NOT DECIDE WHETHER AN ARBITRATION AWARD IS REVIEWABLE TO DETERMINE IF IT IS BASED ON SUFFICIENT EVIDENCE OR IS NOT IRRATIONAL.

Continuing its effort to avoid addressing the question presented, Kowin asserts that this Court has already ruled dispositively on the issue. (Kowin brief at 3, 7) In a strained interpretation of *United Paperworkers International Union v. Misco*, 484 U.S. 29 (1987), Kowin claims *Misco* holds that an arbitration award under the Act is not reviewable for insufficiency of evidence. (*Id.*) *Misco* in no way stands for that proposition.

In *Misco*, an employer sought to uphold the Court of Appeals' vacation of a labor arbitration award rendered pursuant to a collective bargaining agreement. *Misco*, 484 U.S. at 35-36. The employer argued, *inter alia*, that the arbitrator had made erroneous factual findings. *Id.* at 36. This Court rejected that contention and held that arbitration awards were not reviewable for claims of factual or legal error. *Id.* at 36-38.[1]

*Misco* did not even address, much less resolve, the question Eljer has presented here. Rather, *Misco* held that a court could not second guess the *correctness* of facts found by an arbitrator. Here, Eljer does not, and cannot, challenge whether the arbitrator correctly viewed the evidence underlying the extrapolation, because there were no factual findings and there was no evidence.

While the basis for this Petition is a split in the circuits, this Court's decision in *Misco* actually offers some support for Eljer's position. Notably, *Misco* held:

> "To resolve disputes about the application of a collective-bargaining agreement, an arbitrator *must find facts* and a court may not reject those findings simply because it disagrees with them."

---

[1] In contrast to the commercial arbitration at issue here, which is subject to the Federal Arbitration Act, *Misco* concerned a labor arbitration conducted pursuant to the Labor Management Relations Act of 1947. *See Misco*, 484 U.S. at 37 & 40 n.9. Eljer does not challenge the relevance of general arbitration principles from labor arbitrations in commercial arbitrations. However, since the Federal Arbitration Act was not invoked in *Misco*, Kowin mischaracterizes the case as "dispositive" on "whether an arbitration award *under the Act* is reviewable for insufficient evidence." (Kowin brief at 6; emphasis supplied)

*Id.* at 38. (emphasis supplied) This says plainly that construction of the facts is necessary to resolve an arbitration dispute, and suggests there must be some evidence to support an arbitrator's decision.[2]

Kowin's misinterpretation of *Misco* is no more than a ruse by which it seeks to avoid confronting the split in the circuits. The Petition sets forth cases from the Second, Third and Ninth Circuits decided after *Misco* that permit examination of arbitration awards for evidentiary sufficiency or irrationality. *See, e.g., Pacific Reinsurance Management Corp. v. Ohio Reinsurance Corp.*, 935 F.2d 1019, 1025-26 (9th Cir. 1991); *Mutual Fire, Marine & Inland Ins. Co.*, 868 F.2d at 56; *In re Arbitration No. AAA13-161-0511-85 under Grain Arbitration Rules*, 867 F.2d 130, 135 (2d Cir. 1989). Kowin is notably silent with respect to this authority. These decisions are contrary to Kowin's interpretation of *Misco* and also to the Seventh Circuit's ruling.

---

[2] *Misco's* holding is not inconsistent with judicial review of arbitration decisions for sufficiency of the evidence or irrationality. Courts which permit such review recognize that an arbitration decision cannot be overturned for erroneous fact finding. These courts do not examine the correctness of facts found, but simply require the decision to be grounded in *some* facts. *See, e.g., Mutual Fire, Marine & Inland v. Norad Reinsurance Co., Ltd.*, 868 F.2d 52, 56 (3d Cir. 1989); *Storer Broadcasting Co. v. American Federal of Radio & Television Artists*, 600 F.2d 45, 47 (6th Cir. 1979), *cert. denied*, 454 U.S. 1099 (1981).

Review for sufficiency of the evidence or irrationality is also consistent with the longstanding principles that an arbitrator's award must be derived from the essence of the agreement and cannot simply reflect the arbitrator's own notions of justice. (*See* Petition at 18-19).

Kowin does concede that some courts have examined arbitration awards to determine whether the awards were, for example, "unfounded in reason and fact" or "completely irrational." (Kowin brief at 7-8) Yet Kowin claims, without any analysis of the lower court cases, that this Court need not clarify these different standards being used in different circuits, because they are simply different "descriptive phrases" for the same type of review. (*Id.* at 8) The disarray in the circuits is apparent from Kowin's refusal to even acknowledge the contrary authority Eljer advanced from the Second, Third, Sixth and Ninth Circuits (*see* Petition at 10-16), from Kowin's own lengthy inventory of some of the varying standards in use by the lower courts and from the differing results being reached in these cases. (*See* Kowin brief at 7-8)

As both Eljer and Kowin demonstrate, one federal statute—the Federal Arbitration Act—has caused the circuits to develop a host of review standards. Eljer respectfully requests this Court to review the judgment of the Seventh Circuit to ensure that lower courts act consistently as to review for evidentiary sufficiency or irrationality, and to alleviate the increased confusion the Seventh Circuit's judgment would generate as courts and advocates begin to cite and rely on a new and different standard for review.

## CONCLUSION

For all the foregoing reasons, this Court should grant Eljer's petition for certiorari.

Respectfully submitted,

WILBER H. BOIES, P.C.
*Counsel of Record*
DAVID B. BAYLESS
MERCEDES A. LAING
McDERMOTT, WILL & EMERY
227 West Monroe Street
Chicago, Illinois 60606-5096
(312) 372-2000

*Counsel for Petitioner*

Dated: May 27, 1994